

Message Text

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PAGE 01 NAIROB 08667 110751Z

46

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SUBJECT: A PRE-ELECTION LOOK AT KENYAN ECONONMY

REF: NAIROBI 8653

SUMMARY: ELECTIONS HAVE OFFERED GOK POLICY MAKERS AN EXCUSE FOR DELAYING DIFFICULT ECONOMIC DECISIONS NECESSARY IN FACE OF HUGE BALANCE OF PAYMENTS DEFICIT AND RAMPANT INFLATION. AS THESE DELAYS HAVE ALLOWED PROBLEMS TO INCREASE IN MAGNITUDE, STRONG COUNTER MEASURES NEED TO BE TAKEN SOON AFTER ELECTIONS. THEY WILL PROBABLY INCLUDE STRICT IMPORT CONTROLS AND WAGE AND PRICE CONTROLS; A DEVALUATION OF THE KENYA SHILLING IS ALSO POSSIBLE. END SUMMARY

1. KENYA'S BALANCE OF TRADE DEFICIT FOR FIRST SIX MONTHS

1974 WAS \$235 MILLION (AS CONTRASTED WITH \$56 MILLION

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PAGE 02 NAIROB 08667 110751Z

DEFICIT FIRST SIX MONTHS 1973, A PERIOD WHEN IMPORT CONTROLS WERE IN EFFECT). WHILE OIL PRICE INCREASES

CAUSED IMPORTANT PART OF DEFICIT (\$70 MILLION NET OIL DEFICIT VERSUS \$12 MILLION SAME PERIOD LAST YEAR) ALL OTHER CATEGORIES OF IMPORTS ALSO REGISTERED SHARP INCREASES WHICH NOT DUE TO PRICE INCREASES ALONE. TOTAL IMPORTS FIRST SIX MONTHS 1974 JUMPED 95 PERCENT TO \$450 MILLION. EXPORTS SAME PRIOD INCREASED 23 PERCENT TO \$220 MILLION.

2. ALTHOUGH MASSIVE TRADE DEFICIT HAS BEEN EVIDENT FOR SOME MONTHS, NO STEPS HAVE BEEN TAKEN BY GOK TO REDUCE DEFICIT. IMPORT CONTROL PROGRAM WAS ENACTED IN EARLY JUNE THIS YEAR BUT HAS YET TO BE EFFECTIVELY IMPLEMENTED. SHARP CONSUMER REACTION TO SHORTAGES CAUSED BY SIMILAR IMPORT CONTROL PROGRAM IN EARLY 1972 MAY HAVE PROMPTED GOK POLICY MAKERS TO DELAY IMPLEMENTATION OF NEW PROGRAM UNTIL AFTER ELECTIONS LEST THE ELECTORATE, ALREADY DISGRUNTLED BY THE INCREASIFG ECONOMIC GAP BETWEEN THE ESTABLISHMENT AND THE MASSES, BECOMES EVEN MORE RESENTFUL AND EXPRESSES RESEMTMENT BY WHOLESAL DEFEAT OF INCUMBENTS.

3. AT END OF DECEMBER 1973, KENYA'S FOREIGN EXCHANGE RESERVES WERE \$230 MILLION; AT END OF SEPTEMBER 1974 THEY WERE \$170 MILLION. THE SEPTEMBER FIGURE IS \$50 MILLION BELOW RESERVE HOLDINGS END OF JUNE AND INCLUDES DRAWS OF SDR 21.5 MILLION (\$26 MILLION) FROM IMF MADE IN SEPTEMBER. UNLESS DRASTIC ACTION SOON BY GOK, FULL YEAR 1974 PAYMENTS DEFICIT WILL BE BETWEEN \$200 MILLION AND \$250 MILLION, PRIOR TO ADDITIONAL FINANCING FROM IMF AND IBRD WHERE GOK SEEKING \$100 MILLION PROGRAM LOAN.

4. WHILE THE CABINET MEMBERS HAVE BEEN IN THEIR PARLIAMENTARY DISTRICTS PREOCCUPIED WITH ELECTION CAMPAIGN, TOP CIVIL SERVANTS HAVE BEEN FORMULATING PROPOSALS FOR ECONOMIC POLICY TO BE ADOPTED AFTER ELECTIONS. POLICY WHICH IS ULTIMATELY ACCEPTED WILL DEPEND IN PART ON MAKE-UP OF NEW GOVERNMENT, BUT IT OBVIOUS THAT MAJOR POLICY ADJUSTMENTS ARE NECESSARY.

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PAGE 03 NAIROB 08667 110751Z

5. ONE ADJUSTMENT ALMOST CERTAIN OF ADOPTION BY NEW GOVERNMENT IS TIGHT IMPORT CONTROL PROGRAM. THIS WILL HAVE LITTLE EFFECT DURING 1974 AS LICENSES HAVE ALREADY BEEN ISSUED FOR MOST OF IMPORTS WHICH WILL ENTER REMAINDER OF YEAR. NEXT LIKELY POLICY CHANGE IS WAGE CONTROLS TO BE USED IN COMBINATION WITH PRESENT PRICE CONTROLS. WITH INFLATION RATE CURRENTLY 20 PERCENT, WAGE CONTROLS WILL BE EXREMELY UNPOPULAR. A SLOWING OF KENYA'S DEVELOPMENT PLAN IS ALSO UNDER CONSIDERATION; THIS WOULD SLOW IMPORTS AND HELP DAMPEN INFLATION THROUGH CUT IN DEMAND

BY GOVERNMENT SECTOR. DEVALUATION OF KENYA SHILLING
ALSO UNDER ACTIVE CONSIDERATION AND IS INCREASINGLY
POSSIBLE AS MAGNITUDE OF TRADE AND PAYMENTS DEFICIT
BECOMES MORE EVIDENT.
MARSHALL

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